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The impact of distance on SWFs target firms' performance

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Abstract

In recent years, the role of sovereign wealth funds in international financial markets has been drawing the attention of both public opinion and academic research. This work aims at exploring the role of distance as a determinant of SWFs impact on target firms' performance.

Firstly, the work provides an introductory review of the literature on SWFs as investors, including descriptions of the concept, history, typology, investment strategies and concerns raised by their activities. Secondly, a review of existing research on the impact of SWFs' investment on performance is provided, complemented by a chapter about what research has said about distance as a driver of performance in cross-border investment.

Finally, the reviewed topics are brought together in a descriptive and exploratory data analysis that disentangles the dimensions of distance as moderators of SWFs impact on performance.

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Executive Summary

Despite not being new players to the international financial markets, Sovereign Wealth Funds (SWFs) have increasingly been on the spotlight due to the rapid growth of their activity and size. Beyond the debate on the media, the academic world has also turned to SWFs with a focus on two elements: SWFs investment choices and the impact that such choices have on target firms. This work can be placed on the latter group, with a special attention given to the role played by distance as a driver of performance when SWFs engage in cross-border investments.

The work starts with a broad literature review on SWFs showing that simplistic characterisations do not work with this type of investors, as it is reflected by the historic inability of academic literature to provide a clear definition of SWFs. Most definitions share the basic starting point that SWFs are investment vehicles owned and managed by sovereign entities, i.e. states, with organisational independence from central banks or any other public organism. However, SWFs have proven to be a rather heterogeneous group when looked at from different perspectives, such as funding mechanisms or objectives. Findings on investment strategies actually show that SWFs respond to a mix of financial and strategic motivations, the latter being the main source for concerns over their activities. Interestingly, research also shows that SWFs challenge the traditional direction of international investment, as funds based on emerging countries direct vast investments towards developed economies.

The second part of the literature review looks at how the particular nature of SWFs is seen by researchers as an invitation to investigate the impact on the performance of firms in which they invest. Most studies take the approach of assimilating SWFs to potentially equivalent investors, i.e. institutional investors and large shareholders,

underlining the importance of the role played by corporate governance practices. Thus, the scope of SWFs impact on target firms might depend on the degree of activism that funds are willing to assume with regards to monitoring activities or the use of control rights to seek their goals, whether economic or political. The main empirical results are reviewed, finding that most studies are limited to studying the short-term effects on firm value, while empirical work on the long-term implications for operating performance is still scarce.

This work aims to uncover the potential role of distance as a driver of SWFs impact on operating performance. To do so, the main conceptualisations of distance in International Business (IB) are reviewed. By going through the theories on the relationship between distance and performance in cross-border acquisitions, the ground for studying this relationship in the case of SWFs is set.

This is done under an empirical approach by carrying out a brief data analysis. Data is obtained by combining and modifying the databases of two previous works on SWFs. The analysis, which has a descriptive and exploratory nature, finds that while firms' performance does decline after SWFs investment, only some dimensions of distance might be considered to play a moderating role, namely geographic and linguistic distance.

To conclude, the implications of the results are discussed and contextualised as far as managerial and policy implications are concerned, and some directions for further work are provided.

1. Sovereign Wealth Funds

Introduction

The aim of this chapter is to go through relevant existing literature on the roots of sovereign wealth funds (SWFs), in order to provide a deeper understanding of its history, funding, size, investment strategies and the debates around their role in international markets, among other characteristics.

As its name suggests, a SWF is a financial fund owned by a sovereign state, so that national savings are accumulated. The term was used for the first time by Rozanov (2005). It is generally assumed that the main focus of such a fund is on the development of an investment portfolio, often including cross-border investment. Literature provides definitions of SWFs based on their funding, purpose and objectives (Hassan, 2009), but it is still far from becoming a clearly delimited concept.

Since the establishment of the first modern SWFs in the 1950s, they have uninterruptedly grown in number and assets under management (AuM). As shown by Figure 1, managed assets have soared during the last decades as a result of growing currency reserves and the sustained increase of commodity prices, especially since 2003.

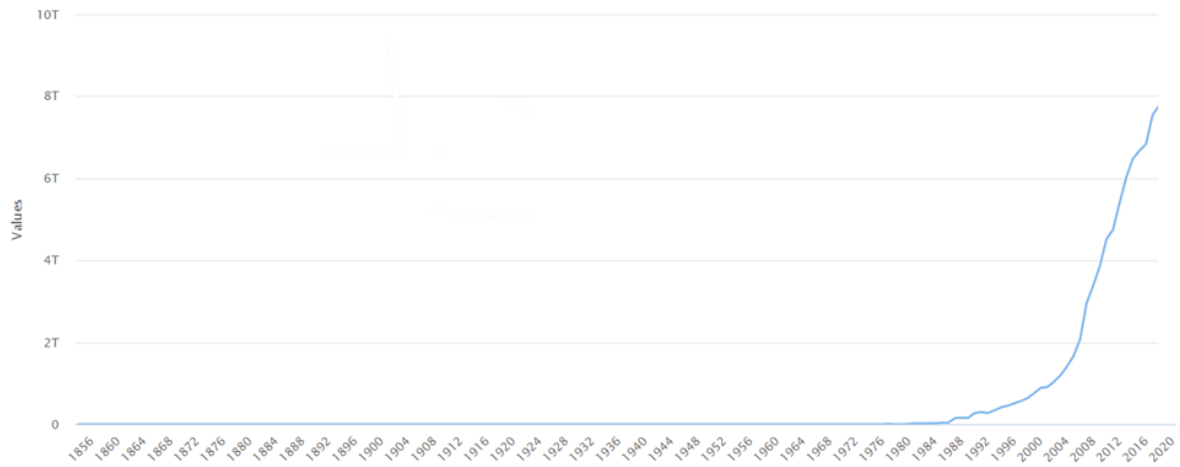

Figure 1. Evolution of total AuM (USD trillion). Source: SWF Institute

According to the SWF Institute, total AuM accounted for over USD 8,4 trillion by the first quarter of 2020.

Due to their ever expanding presence in international markets, SWFs have been increasingly scrutinised by both academic research and public opinion on issues concerning their governance, transparency, investment motivations and accountability. Cross-border acquisitions by SWFs have faced criticism and doubts, as they are often perceived as a threat by the recipient-country governments. Given that SWFs investment tends to flow from developing to developed markets, developed countries are especially concerned by SWFs activities, as it is reflected by episodes such as German Chancellor Merkel's public warning to Russian SWFs on buying European pipelines and other infrastructure.

For all this reasons and more, it is critical to understand the investment behaviour of SWFs and how they impact both international market dynamics and national economies, as well as target firms' governance and performance.

Defining SWFs

Despite lively academic discussion on SWFs, a consensual definition is far from being reached. Academics, international organisms, lawmakers and even sovereign wealth funds themselves have come up with several definitions in an attempt to differentiate them from the heterogeneous category of state-owned financial entities. These include central banks, state-owned enterprises (SOEs), government treasuries or pension funds, among other government-owned entities operating in private markets.

While stabilisation and saving funds have existed for more than half a century, the term "sovereign wealth fund" is a much younger denomination. It was first used by Rozanov (2005) in his article "Who holds the wealth of nations?", where SWFs are defined as

"state-owned investment vehicles aimed at investing national budget surpluses accumulated over the years due to favourable macroeconomic, trade and fiscal conditions, especially from natural resources exports".

Analysing the early literature on SWFs, it could be said that there are at least four different groups, or approaches, to research and definition of the emerging SWF phenomena. As it has been put by some authors (Gelpern, 2010; Xu and Bahgat, 2010), each group shows different motivations for providing SWF definitions, as they choose to emphasise particular aspects. These approaches would be:

SWFs as market participants

Following Rozanov's view, the first comprehensive research reports on SWFs were elaborated by banks and consulting firms, focusing on the growth rate and potential future size of the funds (Farrell et al., 2007; Fernandez and Eschweiler, 2008). Additionally, these reports emphasise the fact that SWFs are not new players but would rather have been active in financial markets for decades. Service providers' definitions of SWFs are aimed to understand their role as market participants by focusing on asset composition and investment strategies.

SWFs seen by recipient-country governments

In early 2008, mainstream media entered the discussion around SWFs, triggering the interest of politicians who needed to know how to react to these developments. Recipient country parliaments and governments elaborated reports to provide legislators with background on the topic, given the increasing pressure from their constituents and the media. Several political organisms provided SWF definitions, such as the Department of Treasury (2007), the US Government Accountability Office (2008) or the European Commission (2008). These definitions mainly focus on the size and

origin of SWFs, also stressing the need to define the scope of possible regulatory measures.

SWFs in academic research

The early academic attempts to define SWFs can be roughly divided in two groups. The first group is composed by authors who focus on analysing the determinants of SWFs' investment and their portfolio management decisions (e.g. Aizenman and Glick, 2008; Balding, 2008). The second group, smaller but highly influential, focuses on the political concerns raised by SWFs operations, especially around transparency and accountability issues. Indeed, they tend to rank the funds according to their performance on these aspects. Some examples can be found on the work of Truman (2007, 2008), Badian and Harrington (2008), and Gilson and Milhaupt (2008), to name a few.

International organisations definition of SWFs

Following a mandate from the October 2007 meeting of the G7 finance ministers and central bank governors, organisms like the World Bank, the OECD and the IMF started publishing a series of reports with the aim of identifying best practices in SWF management and recipient-country behaviour. Accordingly, the IMF included in its February 2008 "work agenda" a more functional definition of the funds by emphasizing different purposes that SWFs may serve (IMF, 2008).

To illustrate the variety of SWF definitions and the four different approaches, Table 1 shows a sample of some of the most influential definitions:

Table 1. Review on significant SWF definitions

YEAR	AUTHOR	SOURCE	SWF DEFINITION or DEFINING CHARACTERISTICS
2005	Rozanov, Andrew	Rozanov, 2005 (State Street Global Advisors)	By-product of national budget surpluses , accumulated over the years due to favourable macroeconomic, trade and fiscal positions, coupled with long-term budget planning and spending restraint. [...] objectives: insulate the budget and economy from excess volatility in revenues, help monetary authorities sterilise unwanted liquidity, build up savings for future generations , or use the money for economic and social development.
2007	Jen, Stephen	Jen, 2007 (Morgan Stanley)	A SWF needs to have five characteristics : (1) sovereign; (2) high foreign currency exposure; (3) no explicit liabilities; (4) high risk tolerance; and (5) long investment horizon.
2007	Lyons, Gerald	Lyons, 2007 (Standard Chartered Bank)	Their main characteristics are: ownership by a sovereign nation state rather than a regional or local state entity; not national pension funds and not central banks or authorities that perform roles typical of a central bank.
2007	US Dept. of Treasury	Department of Treasury, 2007	A government investment vehicle which is funded by foreign exchange assets, and which manages those assets separately from the official reserves of the monetary authorities (the Central Bank and reserve-related functions of the Finance Ministry). SWF managers typically have a higher risk tolerance and higher expected return than traditional official reserve managers.
2007	Kern, Stephen	Kern, 2007 (Deutsche Bank)	Financial vehicles owned by states which hold, manage or administer public funds and invest them in a wider range of assets of various kinds. Their funds are mainly derived from excess liquidity in the public sector stemming from government fiscal surpluses or from official reserves at central banks
2008	US Govt. Accountability Office	US Govt. Accountability Office, 2008	Funds that (1) [are] government chartered or sponsored investment vehicles; (2) invested, in other than sovereign debt, some or all of their assets outside the country that established them; (3) [are] funded through transfers from their governments of funds arising primarily from sovereign budget surpluses, trade surpluses, central bank currency reserves, or revenues from the commodity wealth of the countries, and (4) [are] not currently functioning as pension funds receiving contributions from and making payments to individuals
2008	Fernandez, David G. Eschweiler, Bernhard	Fernandez and Eschweiler, 2008 (JPMorgan)	Special government asset management vehicles which invest public funds in a wide range of financial instruments. Unlike central banks, which focus more on liquidity and safe-keeping of foreign reserves, most SWFs have the mandate to enhance returns and are allowed to invest in riskier asset classes , including equity and alternative assets [...]
2008	Miracky et al.	Miracky et al., 2008 (Monitor)	A government investment vehicle that meets three criteria: (1) It is owned by a sovereign government (2) It is managed separately from funds administered by the [...] central bank, ministry of finance, or treasury (3) It invests in a portfolio of financial assets of different classes and risk profiles, including bonds, stocks, property, and alternative instruments, with a significant portion of assets under management invested in higher-risk asset classes in foreign countries
2008	International Monetary Fund	IMF, 2008	Government-owned investment funds set up for a variety of macroeconomic purposes . They are commonly funded by the transfer of foreign exchange assets that are invested abroad with a long-term horizon.
2008	International Working Group of Sovereign Wealth Funds (today, IFSWF)	IWG, 2008	Special purpose investment funds or arrangements owned by the general government. Created by the general government for macroeconomic purposes, SWFs hold, manage, or administer assets to achieve financial objectives, and employ a set of investment strategies which include investing in foreign financial assets. The SWFs are commonly established out of balance of payments surpluses , official foreign currency operations, the proceeds of privatizations, fiscal surpluses , and/or receipts resulting from commodity exports.
2010	Bortolotti et al.	Bortolotti et al., 2010 (Monitor/FEEM)	An investment fund that meets five criteria: (1) It is owned directly by a sovereign government. (2) It is managed independently of other state financial institutions. (3) It does not have predominant explicit pension obligations. (4) It invests in a diverse set of financial asset classes in pursuit of commercial returns. (5) It has made a significant proportion of its publicly-reported investments internationally.
2015	Alhashel	Alhashel, 2015	Investment funds which have the peculiarity to be owned by a state.

Paying attention to the elements on which each of the groups puts the emphasis, it can be argued that a definition for SWFs generally revolves around the following characteristics:

Ownership

Despite a common starting point according to which a SWF is by definition owned by a public political institution (i.e. a government), there is a variety of opinions regarding whether it should also include sub-national governments' ownership (i.e. federal states, administrative regions). The point that sub-national entities do not qualify as "sovereign", meaning they may not have the decision rights associated with central governments, has often been made (Monitor, 2010). However, evidence shows that sub-national SWFs do exist (e.g. Alaska Permanent Fund, Alberta Heritage Savings Trust Fund), and even the International Forum of Sovereign Wealth Funds (IFSWF) includes two sub-national funds among its members[1]. Consequently, the general practice and the one that will be followed in this work is to equally treat sub-national and national SWFs, as both face the same issues when performing cross-border investments.

Funding sources

Many definitions provide a list of possible funding sources for SWFs, which generally fall into three categories: fiscal sources, foreign reserves and commodity sources (Fernandez and Eschweiler, 2008). However, it must be said that most definitions claim that these sources must be strictly *public* and that funds must not have explicit short-term liabilities attached to them. The only exception of the latter would be that of pension funds, which are funded from individual contributions that bind them to direct

[1] Alaska Permanent Fund and Abu Dhabi Investment Authority (according to information retrieved from IFSWF website on April 2020)

liabilities towards beneficiaries. For this reason, there is a long-lasting controversy on whether pension funds should be defined as SWFs.

Purpose

Some definitions enumerate potential objectives which SWFs might pursue. Beyond that, it must be emphasised that SWFs tend to seek multiple, changing and seldom overlapping objectives. Using IMF (2008) definition, SWFs can be distinguished based on their main goal(s), namely: stabilisation funds, saving funds, reserve investment corporations, development funds and contingent pension reserve funds. Later literature has usually combined these objectives under the name of "macroeconomic purposes", also aiming to differentiate SWFs from specialised public funds with a very narrow mandate (e.g. those exclusively dedicated to infrastructure financing).

Management and investment style

Another characteristic of SWFs which has usually been included in literature definitions is their propensity to engage in long-term investments with a generally higher risk and lower liquidity than those of other institutional investors, such as central banks or pension funds (Das, Mazarei and Van der Hoorn, 2010).

History of SWFs

It can be said that the emergence of sovereign wealth management is connected to the will of giving a structure to sovereign wealth to better exploit its financial possibilities, while still keeping it under the control of the state. From this perspective, a precursor is found in the colonial British East India Company, whose revenues derived from taxation in British colonies. However, both the British state and private shareholders would benefit from dividends, a situation which clearly diverges from modern SWFs, which are wholly-owned by the government. A more accurate precursor of modern SWFs can be

found in the 1816-born French Caisse des Dêpots et Consignations (CDC), being a state-backed, public deposit-taking institution designed to provide benefits for the broader public. It later developed into a government holding company, much before than modern equivalents like Singapore's Temasek or the Russian Direct Investment Fund.

However, it wasn't until the 1950s that the first modern SWFs were created under British colonial administration: the Kuwait Investment Authority (1953), and its predecessor the Kuwait Investment Board (1945), followed by the sovereign fund of Kiribati (1956). The 1970s and 1980s saw the creation of several SWFs, rather heterogeneous regarding its purpose and set-up, ranging from oil- and other natural resource-based funds to government holding companies. Some examples are Singapore's Temasek fund (1974), the Abu Dhabi Investment Authority (1976), the Oman Investment Fund (1980), the Brunei Investment Agency (1983) or the Norges Bank Investment Management Fund (1990). The latter has grown to become the largest SWF in the world.

Both the number of SWFs and their size in term of assets value have continued to grow uninterruptedly during the 90s and into the 20th century, until our days. Up to 46 new SWFs were established from 2000 to 2009. As a response to the 2008 financial crisis, some countries decided to build some reserves by creating new SWFs or increasing the value of existing ones. According to a report by IE Business School (ICEX – Invest in Spain and IE Business School, 2018), 31 new SWFs were created between 2010 and 2016 and, by the end of 2018, up to 18 countries were considering establishing a new fund. The total number of SWFs by the end of the decade stands near 100.

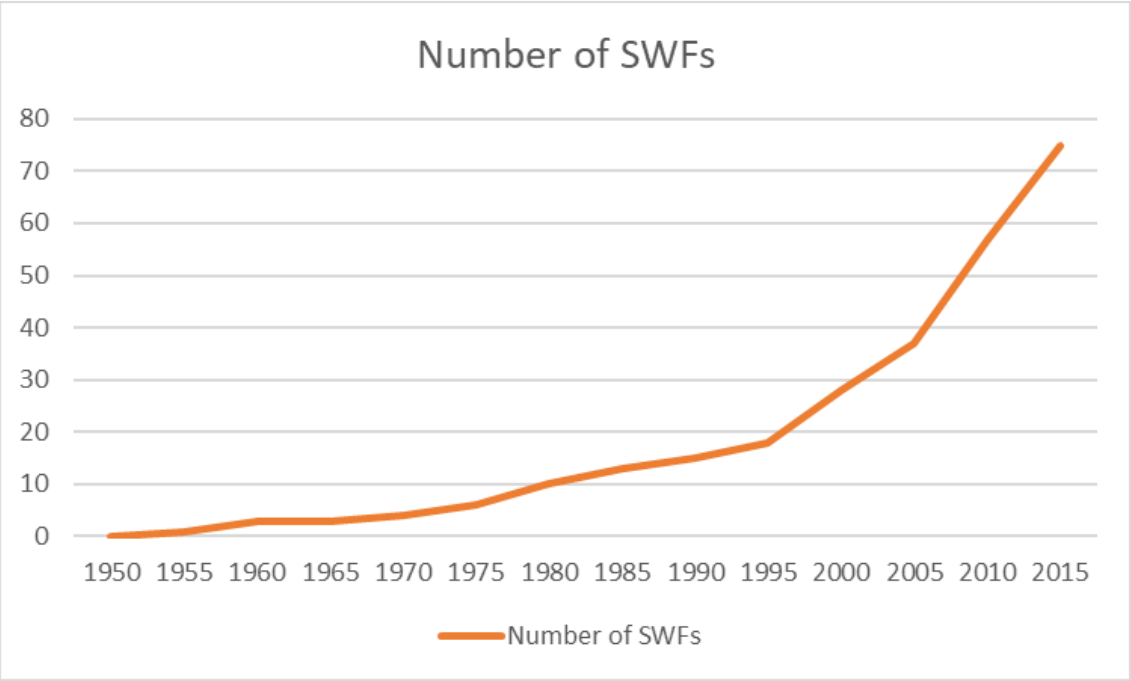

Figure 2. Evolution of the number of SWFs since the 1950s (SWF Institute, 2018; Airoldi and Lidgard, 2018)

Classification of SWFs

As discussed in the SWFs definition chapter, SWFs possess several traits that are common to all funds. However, SWFs are at the same time far from being a homogeneous group, showing notable differences in their behaviour as market participants. Legal frameworks, macroeconomic objectives, risk management, funding mechanisms and transparency, just to name a few, are some the aspects in which they are diverse. As Xu and Bahgat (2010) wrote, "the extent to which sponsoring governments differ with regard to social, political and economic issues, so will differ their respective funds". The following pages provide an analytical approach to SWFs categorisation based on three of their characteristics: funding sources, objectives and investment strategies.

SWFs by funding sources

According to Fernandez and Eschweiler (2008), SWFs are funded with three main types of assets:

- Revenues from sales of natural resources
- Excess foreign exchange reserves
- Fiscal surpluses

It is interesting to say that these assets generally accrue in foreign currency, with the partial exception of fiscal sources.

Revenues from natural resources (or commodity-driven funds)

Natural resource revenues are the funding source for a major number of SWFs. They are expected to be so also for a majority of the planned sovereign funds, as most of them belong to natural resource-rich African countries. Most of the revenues derive from hydrocarbons (oil & gas), while others derive from a mix of commodities including other hydrocarbons, metals and minerals.

Excess foreign exchange reserves

It is the second most important source for SWFs' funding. An important characteristic of funds financed with foreign exchange reserves is that they tend to be notably larger than natural resource funds. This is mainly because they generally get a single and large initial transfer from the country's reserves, while commodity-funded SWFs grow progressively as natural resources income is transferred to the fund over an extended period of time. However, the evolution of assets under management shows that foreign exchange-funded SWFs grow at a much slower pace than their resource-funded peers, explaining

why long-standing commodity funds have grown to cope the top positions in total asset rankings.

Fiscal surpluses

A third major funding source for SWFs comes from government contributions from fiscal surpluses, to which proceeds from the sale of public assets or direct transfers of government-held assets are added. Despite a majority of funds in this category are seen as relatively transparent compared to resource-driven funds (Linaburg and Maduell, 2011), attempts to provide a reliable asset valuation come up with the challenge of having a large share of illiquid assets. It is usual for these funds to be categorised as government holding companies (e.g. Temasek, SCIC,EIA[2]), as they are often handed over the management of state-owned enterprises (SOEs) or government participations in privatised companies. This is also the category were pension reserve funds are found, if considered SWFs, since they are funded by transfers from national public budgets.

SWFs by purpose

As it has been briefly discussed in previous chapters, SWFs differ in their objectives. In addition, some complexity is introduced by the fact that a SWF might have several objectives that overlap and change over time. As an example, the Kiribati sovereign fund was created as a stabilisation vehicle to protect national economy from inflation and fluctuations on natural resource prices. However, as phosphate reserves have progressively decreased, the fund has been transformed to seek a return-oriented portfolio. Clark and Monk (2011) show that the same can be said from several originally

[2] SCIC: State Capital Investment Corporation (Vietnam); Emirates Investment Authority (United Arab Emirates)

oil-funded Middle Eastern SWFs, which have constantly adapted their targets due to changing national and international contexts. Failure in operationalising and implementing the objectives has also been a reason for change, as in the case of Nauru, whose SWF is currently dependent on international donors after having consumed the original phosphate-based wealth.

Despite the challenge posed by multiple and changing SWFs purposes, scholars generally agree in identifying five major economic objectives. According to this objectives, the Sovereign Wealth Fund Institute and the IMF (2008) propose the following categorisation:

- Stabilisation funds
- Pension reserve funds
- Inter-generational savings funds
- Reserve investment funds
- Strategic development funds

Stabilisation funds

They aim at protecting the national economy from volatility in commodity prices. By nature, a majority of natural resources-funded SWFs have a stabilisation purpose (Das et al., 2009). Stabilisation focus can be placed either on macroeconomic or fiscal aspects. On the one side, macroeconomic stabilisation refers to mechanisms that avoid inflationary pressure and appreciation of real exchange rates (Das, Mazarei and Van der Horn, 2010). On the other side, funds seeking fiscal stabilisation try to smooth the impact of volatile natural resources income on government spending by accumulating wealth during periods of high natural resource prices. Norway's Government Pension Fund Global (GPFG) is a best practice example, as it is fully integrated into the country's

fiscal processes, playing a relevant role in both balancing budgets and avoiding an overheating of the national economy through diversified cross-border investments. Chile's Economic and Social Stabilisation Fund and the Kuwait Investment Authority (KIA) are additional examples of funds with a clear stabilisation mission.

Pension reserve funds

This type of SWFs aims at providing for "contingent unspecified pension liabilities from sources other than individual pension contributions" (Das, Mazarei and Van der Hoorn, 2010). They mirror the expectations about a nation's future pension shortfall and, consequently, they are usually given a clear return target as a function of assumptions about the time and magnitude of such eventual shortfalls. They are mostly found in countries with a mature economy and, more specifically, where demographic pressure is mounting. Some examples are Ireland's National Pension Reserve Fund, the Australian Future Fund and Norway's GPFG.

Inter-generational saving funds

In order to protect the interests of future generations, SWFs can be mandated to operate according to rules which guarantee that present resource income is transformed into future financial cash flows (Das et al., 2009). Inter-generational funds provide clear rules on withdrawals for fiscal purposes and, on some occasions, guidelines for long-term oriented strategic asset allocation that favour investment diversification abroad. It can be argued that most SWFs share an inter-generational savings mission. The most relevant savings funds are the Abu Dhabi Investment Authority, the Qatar Investment Authority and again the multi-faceted Norway GPFG, all of them resource-driven, despite some foreign exchange reserves-driven funds might also have a saving objective.

Reserve investment funds

The mission for reserve investment funds is to improve financial returns of excess foreign exchange reserves. Consequently, it is the typical objective that governments set to excess reserve-financed funds which receive punctual transfers from central banks' balance sheets. By being fully independent from central banks' books, reserve investment funds seek returns beyond standard central bank portfolios, meaning that higher risks are taken in comparison to what would be permissible for central banks. Some examples of such type of funds are Singapore's GIC, the Chinese Investment Corporation (CIC) and the Korean Investment Corporation (KIC), while Botswana's Pula Fund represents a very notable exception as it remains on the central bank's balance sheet.

Strategic development funds

Development objectives are given to funds in order to help strengthen the funds' domestic economies. The fact that their investment might be located completely on the domestic economy is a reason to question whether these funds qualify as SWFs. Santiso (2008) argues that development funds investing both domestically and in developing countries might be considered as a specific type of "sovereign development fund", adding that SWFs increasing investment on emerging economies may reflect the growing importance of development goals. Beyond the debate, the fact that domestic development goals are given to some SWFs as a secondary mission is an objective fact (e.g. Qatar Investment Authority, State Oil Fund of the Republic of Azerbaijan).

Geographical distribution of SWFs

In terms of geographical distribution, four regions dominate the SWF landscape if both number of funds and volume of AuM are considered: Asia Pacific, the Middle East, North

America and Europe – this latter group mainly dominated by the gigantic Norwegian sovereign fund (GPFG). The first two regions represent two thirds of the total assets managed by SWFs around the globe, a dominance which is strongly related to the combined effect of sustained above-average economic growth in emerging economies and price hike across most commodities during the last two decades. Despite the fact that the biggest SWF is by far Norway's GPFG, with a total assets value closing in on USD 1,2 trillion as per March 2020, Western countries generally are minor players in the global sovereign wealth paradigm.

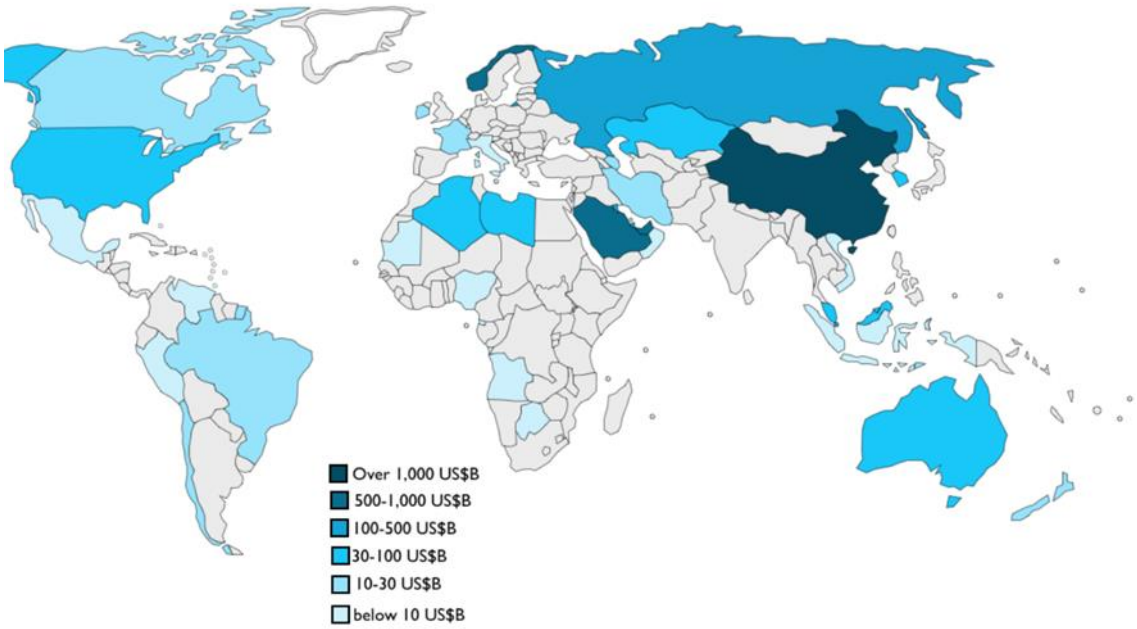

Figure 3. Largest SWF distribution around the globe by AuM (SWF Institute, 2020)

According to PWC's Annual Report on Sovereign Investors (2020), current international economic trends set the ground for expected growth of SWFs in Asia Pacific, the Middle East and Africa, with Sub-Saharan funds expected to show tremendous growth in terms of percentage. Considering current plans on SWF creation, this region is also expected to generate an increasing number of commodity-driven funds which could account for

up to a third of newly created entities in the years to come. However, total assets at a global level are expected to show more moderate growth figures.

SWFs investment strategies

Despite the fact that SWFs investment choices are affected by a variety of factors, it can be said that the objectives which they are set to pursue constitute the main determinant of strategy. Objectives themselves depend on economic factors (e.g. funding sources) and political preferences. Commodity-based SWFs, for instance, tend to be under strong stabilisation mandates which favour diversified investments abroad with long-term horizons. In this way, steady revenue streams are provided avoiding any overheating or crowding-out in the domestic economy.

According to Bernstein, Shai, and Schoar (2009), three major categories for SWFs perspectives can be identified:

- The *development perspective* suggests that funds would direct their investment towards strategic long-term projects, aimed at maximising broader social objectives rather than pure financial returns.
- The *political perspective* would favour investments with a clear political agenda that would benefit the governments, the party or even the individual politician's interest.
- The *agency perspective* argues, very similarly to the development perspective, that funds are set to engage in activities which maximise community welfare, but can generate agency costs, corruption and misallocation.

The authors analyse a total number of 2662 SWF deals between 1984 and 2007, concluding that investment strategy depends on the ultimate decision makers, i.e.

political leaders or professional managers, concluding that governance structure is a determinant of the funds' objectives, investment strategy and performance.

Bortolotti et al. (2010) propose two rationales behind SWFs investment patterns depending on the activism in which SWFs are willing to engage as investors. On the one hand, SWFs can act as passive investors, a behaviour that the authors relate to negative performance and loss of value. On the other hand, an active role by SWFs combined with long-term horizons and large-stake acquisitions would benefit both the SWF and the recipient firm in terms of performance and value. The impact on performance and value will be further discussed in the present work.

Regarding the issue of SWFs' investor activism, the IMF identifies three SWF investor categories (Das, Mazarei and Van der Hoorn, 2010):

- *Conservative passive investors* follow a liquidity-oriented investment strategy focused on capital preservation. This category of funds hold portfolios characterised by fixed-income assets, short-term investment horizons and low risk profiles, while maintaining a globally balanced asset allocation. It is the case of several SWFs with reserve investment or stabilisation objectives, including the Russian Reserve Fund, KIA, GIC and CIC.
- *Yield-seeking passive investors* run highly diversified portfolios with longer investment horizons which allow for higher risk. A typical investment portfolio for this type of funds would include holding a notable share of equities abroad, while also targeting both fixed-income assets and higher-risk investments (e.g. hedge funds, real state or private equity). Many inter-generational savings and contingent pension reserve funds fit in this category, as they pursue more illiquid investment strategies. Norway's GPFG and ADIA – the two biggest SWFs in the

world – are found in this category, together with smaller ones such as the Australian Future Fund and the Irish National Pensions Reserve Fund.

- *Strategic active investors* constitute the smallest yet relevant category. It is a rather heterogeneous group including very active investors like the QIA[3], private equity-like investors such as Mumtalakat (Bahrain) and Mubadala (Abu Dhabi), and also government holding companies such as Malaysia's Khazanah or Singapore's Temasek. It is typical for this kind of funds to adopt an asset-seeking perspective, as they target international assets which would potentially yield benefits for domestic economic and technological development.

Other attempts to understand SWFs investment strategies concerns the position that they hold among government investment vehicles. The management consulting firm Monitor developed a framework that conceptualises a continuum of government investment vehicles depending on two variables, risk appetite and liquidity (Monitor 2008).

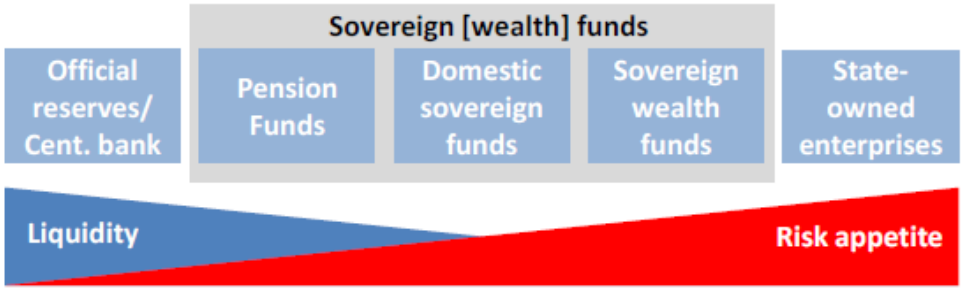

Figure 4. Monitor SWF continuum (Monitor 2008)

As shown in Figure 4, central banks would be placed at one end of the continuum as they manage official reserves with a liquidity-oriented and risk-averse perspective, while

[3] Qatar Investment Authority

state owned enterprises (SOEs) engaged in riskier, illiquid investments would be on the opposite end. In the middle, three different sovereign wealth investment vehicles are found, namely pension funds, domestic sovereign funds and SWFs, understanding the latter as foreign currency-denominated funds. This approach helps characterise the investments in which SWFs engage and emphasises their hybrid nature, not qualifying as being neither an official public institution nor a state company.

An additional framework is proposed by the investment management firm Invesco, according to which SWFs investment strategies respond to four different profiles based on the funds' primary and secondary objectives (Invesco, 2011). On the one hand, SWFs primarily focused on development goals may have a domestic or cross-border orientation. This would differentiate pure *development agencies* from funds that support a foreign policy agenda by investing in development projects abroad. One the other hand, SWFs with a clear financial investment orientation, may choose between portfolio diversification and pursuing the maximisation of risk/reward ratios. The tree diagram shown in Figure 5 illustrates this taxonomy of SWFs investor profiles.

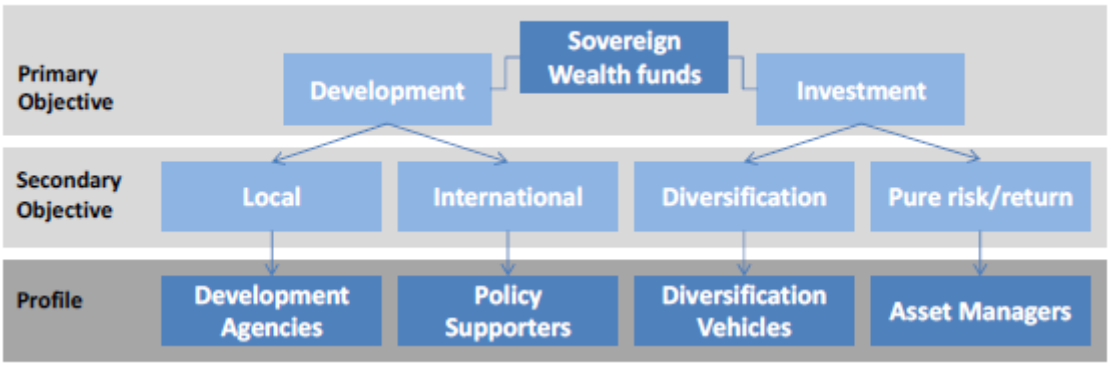

Figure 5. SWF investor profiles as proposed by Invesco (Invesco, 2011)

Overall, it can be concluded that the variables describing SWFs investment strategies are not very different from the dimensions commonly used for a broad majority of investors. A possible list of continuous investment variables are:

1. Time horizon (short-term vs. long-term)
2. Risk profile (risk-averse vs. risk-seeking)
3. Asset allocation (traditional vs. alternative)
4. Product structure (direct investing vs fund investing)
5. Geographical scope (domestic vs. international)

Notably, the particularity of SWFs investment strategies would be rather related to the political interests which might eventually hide behind investment choices.

Concerns around SWFs activities

Major concerns about political motivations behind SWFs investment choices have been raised in parallel to their growth in terms of number and managed assets. In May 2007, Chinese SWF CIC's bid on American investment fund Blackstone hit the headlines of major media, especially given the size of the transaction (USD 3 billion). In the same year, an article in the Financial Times by former US Secretary of the Treasury Larry Summers claimed that SWFs "shake the logic of capitalism", a view supported by Gilson and Milhaupt (2008) in their definition of SWFs as "neo-mercantilist institutions using company-level behaviour to maximise country-level economic, social and political benefits". Also in 2008, even a then presidential candidate Barack Obama commented during his campaign on his personal concerns about SWFs being motivated by more than just markets considerations. He literally said: "That's obviously a possibility".

Beyond the public opinion debate, many scholars have tried to assess the extent to which SWFs operations are mainly driven by financial criteria and to what degree they reflect political agendas. The question to be answered is whether strategic political goals are pursued along with financial ones.

Some researchers claim that SWFs are generally governed according to investment efficiency standards. In an analysis of foreign and private equity transactions undertaken by SWFs, Balding (2008) underlines an absence of non-economic investment motives. Nevertheless, he conceded some credibility to suspicions around SWFs political agendas by recognizing that "the logic behind the fear is not irrational", given the historical evidence of SWFs role as instruments of state power. In a more categorical tone, Loh (2010) affirms that anti-SWF concerns are only the result of not understanding the role of SWFs as investors, as no clear evidence of SWFs acting under purely political motives has been found. This is aligned with earlier work by Epstein and Rose (2009), who advised to consider that SWFs are market-driven as a prudent default assumption, given the lack of contradictory evidence.

However, a majority of the existing research papers claim that interests driving SWFs management are not entirely economic, providing a diverse set of explanations. Chhaochharia and Laeven (2008) find that SWFs often invest to diversify away from industries in the domestic economy and mainly in countries which share a similar culture, suggesting that their investment rules might not be entirely driven by return maximisations but hide some political motivations.

Clark and Monk (2011) characterise SWFs' investment choices as the result of both the fund and the nation's strategic interests. In addition, they suggest that the ruling elites of a country and SWF managers sometimes show conflicting interests, as the former try

to impose their political agenda over the fund's management criteria. Concerning the role of political elites, Hatton and Pistor (2011) observe that the prevailing objective of SWFs from non-democratic countries like China, Singapore, Kuwait and Abu Dhabi is to maximise political gains. They propose the "autonomy-maximisation theory", which identify ruling elites as the true stakeholders of the funds, which become "a valuable tool for protecting their interests; mainly their privileged position". This stand is logically very much dependent on political stability and corruption in the home country, meaning that SWFs may also be understood as an instrument serving the state's general interests. Knill, Lee and Mauck (2012) assume that political relations do matter in SWFs' decision-making processes. They also provide empirical evidence showing that SWFs behave differently than rational investors in relation with the risk/reward trade-off.

In an attempt to provide a framework for political concerns around SWFs, Truman (2010) provides a list of five types of concerns:

1. Mismanagement of investments by SWFs to the economic and financial detriment of the domestic country itself.
2. Pursuit of political and economic power objectives through SWF.
3. Financial turmoil and uncertainty associated with SWFs activities.
4. Conflicts of interest between SWFs' home countries and the investee countries.
5. Exacerbation of financial protectionism inspired by SWFs.

Finally, it is worth mentioning the growing importance of transparency assessment on SWFs activities, reflecting that the potential political bias of SWFs has become the general assumption. As Truman (2010) put it, "SWFs are political by virtue of how they are established, and by their nature are influenced to some degree by political considerations". The most commonly used SWF's transparency indexes are Truman's

and Linaburg-Maduell's, the latter being sponsored by the Sovereign Wealth Fund Institute. The need for transparency has even been positively received by some SWFs, such as the Norwegian GPFG, which in its own statements admit that non-financial motivations influence their investment decisions. Indeed, they have actually set some rules according to which the fund cannot invest in targets not compliant with predefined transparency, labour and environmental standards. Even a list of excluded companies with the exclusion justification is provided on their website.

All of the exposed concerns about transparency and SWF practices explains 2008 IMF's initiative to develop a set of guidelines according to which SWFs need to be managed. Under the name of *Generally Accepted Principles and Practices* (GAPP), best known as the Santiago Principles, a list of principles was drafted with the cooperation of the 23 member states of the IWG. The principles include requirements to provide information on SWFs objectives, their legal and institutional frameworks, alignment with macroeconomic policies, governance structure and their investment and risk management framework. As Kratsas and Truby (2015) underline, these are not utopian requirements, but a list of basic best practices that some SWFs were already following at the time of adoption. Some SWF-specialised researchers have criticised that the principles "are not rigorous enough as outsiders would prefer" and "not explicit about what information should be publicly disclosed" (Bagnall and Truman, 2013). Moreover, adherence to the GAPP is voluntary and no enforcement mechanism is provided, a situation that is reported to have allowed for a "sluggish" (Behrendt, 2010) and "slow, incomplete compliance with the principles" (Dixon, 2014).

2. The impact of SWFs investment

During the last decades, research on SWFs has been conducted in two different directions. The first one, and probably the most prolific in terms of research volume, has been the study of SWFs market selection. Through the analysis of SWFs investment choices, researchers have tried to detect patterns in an attempt to better understand the internationalisation strategies that SWFs put in practice. The second path of research tries to clarify whether SWFs impact on target firms is not only significant, but also if it is in any way different from the impact of other kind of investors. This work can be placed in the latter group of research.

The role of SWFs as investors and the way in which they impact target firms is not clear, since they can be a source of both benefits and costs.

In the case of cross-border investment, SWFs can be seen as a form of foreign direct investment (FDI). Research on MNEs and internationalisation effects show that firm value might increase when receiving FDI due to improved access to knowledge, markets, patents or consumer goodwill, among other intangible assets (Görg and Strobl, 2001; Gozzi, Levine and Schmukler, 2008).

Political connections can have both positive and negative effects on target firms' value and performance. SWFs investing in domestic firms might be in the position of influencing or anticipating governmental policies, putting them in an advantageous position in the market. Indeed, empirical evidence shows that firms with political connections with domestic governments tend to earn higher market returns as a result of preferential treatment (e.g. Fisman, 2001; Goldman, Rocholl and So, 2009; Faccio and Parsley, 2009; Bunkanwanicha and Wiwattanakantang, 2009). There is lesser evidence for this effect in the case of cross-border acquisitions because of governmental influence

being limited outside of the domestic economy. In fact, shareholders related to foreign government might force the firm into sub-optimal decision-making that would benefit the interests of the investing country. This view is connected to the effect of political interests when they are dominant over purely financial or managerial criteria, which is a major concern when SWFs hold a significant control on firms' corporate governance.

In this chapter, I will provide with a review on the academic literature on the topic of SWFs impact on firm value and performance, paying attention not only to the findings but also to the diversity of approaches.

Literature review on the impact of SWFs investment

Financial and operating performance

In the attempts of existing literature to study the impact of SWFs on firms, performance has been looked at from two different perspectives, those being financial and operating performances.

Performance has been mostly studied by assessing the effect on firm value, that is, financial performance. Most papers on the matter have used measurements of cumulative abnormal returns (CAR) to check whether firm value is affected by the announcement of a SWF acquisition. The results have proven to be generally significant, providing support for the idea that SWFs investment is related to an increase in the target firm's stock return due to the expectation of a positive effect on the firm's overall performance. Such significant and positive stock price variation has been quantified in a

range from 0.5% to 2.0% by four concurrent papers (Kotter and Lel, 2009; Bortolotti et al., 2010; Knill, Lee and Mauck, 2012; Chhaochharia and Leaven, 2008)[4].

There is a systematic lack of studies on the impact of SWFs on firm operational performance, if compared to financial performance. Sojli (2010) investigates changes in firm value, profitability and efficiency. Taking EBITDA/sales and EBITDA/assets as indicators for the latter two, it concludes that target firm performance experience a significant improvement in the two years after SWF investment. They find these results to be aligned with the findings for other type of investors, such as hedge funds (Brav et al., 2008), also sustaining that the increase of performance caused by SWFs investment is higher than those of hedge funds and passive investors.

In the same direction, Fernandes (2014) shows how value creation is boosted by SWFs ownership, by measuring a long-term increase on ROE, ROA and EBITDA/assets. The author proposes three different reasons for which SWFs induce improved operating performance: stronger monitoring effects, better access to capital, especially when an important stake is acquired, and improved access to foreign product markets.

An original viewpoint is adopted by Del Giudice, Marinelli and Vitali (2014), as they apply network theory discipline in the analysis of financial markets to dig in the impact of SWFs on target firms operating performance. From this perspective, connections between firms targeted by the same SWF have a positive effect on these firms operating performance. Taking ROA as an indicator for performance, the authors find that highly

[4] It is relevant to say that each of them responds to a slightly different focus. Kotter and Lel (2009) study the effect in the case of financially struggling target firms. Bartolotti et al. (2010) look at both short and long-term returns for a sample of listed target companies. Knill, Lee and Mauck (2012) focus on changes on both returns and risk indicators after SWFs acquisitions. Chhaochharia and Laeven (2008) consider cultural bias in SWFs investment portfolio.

central firms in a SWF's network of target firms enjoy better results, as a consequence of better access to information, deal flow, expertise and contacts. Additionally, they check for other factors that significantly explain higher operating performance, such as larger stakes acquired, direct investment rather than subsidiaries or investment vehicles and targeting domestic firms rather than foreign ones. Finally, they find an interesting concave relationship between the number of SWFs investing in a firm and its operating performance. The latter finding suggests that network theory application to the study of SWFs impact could be a path for further research on the topic.

Similarities with other types of investors

An important volume of research has taken the approach of assimilating SWFs to other type of investors, the most usual ones being institutional investors and large shareholders.

Literature on institutional ownership and shareholder activism shows conflicting views over the extent to which investor activism facilitates improvement in target firms' values, earnings, operations and governance structures (Karpoff, 2001). Some papers find that institutional investors like pensions funds do successfully perform monitoring and promoting changes in target companies (Del Guercio and Hawkins, 1999). However, not a low number of works qualify institutional investors as largely ineffective monitors failing to boost shareholder value through monitoring activities (Gillan and Starks, 2000). Carleton et al. (1998) and Woidtke (2002) elaborate on institutional investors' inadequate monitoring skills and bring in the argument that their objectives tend to be in conflict with value maximisation, providing an additional reason for which this kind of investors contribute to firm performance reduction. Just a few authors find evidence for

the ability of institutional investors to improve firm value through monitoring activities (e.g. Smith, 1996). Nevertheless, it must be said that some researchers defend a more balanced approach according to which the impact on firm value is variable depending on institutional investor size and independence. Their conclusion is that large investors are more likely to engage in monitoring activities and that firms participated by independent institutional investors receive higher valuations, in contrast to funds with strong institutional or political connections (Ferreira and Matos, 2008; Gianetti and Laeven, 2008).

Considering that SWFs are generally large government-connected investors, these findings need to be considered ambiguous in relation to their impact on firms. Kotter and Lel (2009) specifically test the similarity of SWFs and the wider category of institutional investors. They conclude that they share very similar investment preferences for target firms' characteristics and that both of them have a positive effect on firm value around the date of announcement. However, long-term firm performance and corporate governance outcomes are not found to be substantially affected by SWF investment.

The possibility of assimilating SWFs impact on firm performance to that of large shareholders is the most common context under which the matter has been looked at. When assessing the impact of large investors on firm performance, shareholder activism becomes a key factor, since the scope of such impact is eminently affected by the extent to which the investor is engaged in corporate governance activities.

It is often argued that SWFs generally behave as passive investors. In fact, some SWFs have refused to take board seats when they have been offered to do so, partly because

of political pressure[5]. Bortolotti et al. (2010) also support the idea that SWFs are passive investors, noting that they generally do not ask for seats on the board of directors after acquiring a significant stake, and try not to interfere in managerial decisions so that political opposition and regulatory backlash in the target firm country are avoided. In consonance with these observations, Mehropouya et al. (2009) insist that SWFs seldom come up with resolutions to be voted and tend to support management decisions.

In the already mentioned paper by Kotter and Lel (2009), the authors find that SWFs investment behaviour and their effect on target firm performance are consistent with those of passive institutional shareholders. They also examine the relationship between a proxy of activism (CEO turnover) and target firm operating performance, finding no evidence for the idea of SWF activism, at least if compared with other investors.

However, the analysis becomes quite different when the possibility of SWFs usually behaving as active investors is considered. Opposition to management positions, usual communication with firm management, submission of shareholder proposals, together with backstage private negotiations with management are some examples of investor active behaviour. Actually, despite having an image of being mostly passive investors, the combination of large stake size and long investment horizons justifies a natural tendency towards investor activism for SWFs (Ghahramani, 2013). Monitoring is regarded as the predominant activity performed by active SWFs, and the one about which more literature has been produced. However, there are eventually more efficient

[5] As an example, in 2007 the China Investment Corporation refused a seat in Blackstone Group's board, despite holding a US$ 3 billion stake. In 2008, the Government of Singapore Investment Corp. was offered a board seat in UBS, being its largest shareholder, but also refused to take it.

channels through which SWFs can add value to the firm. Dewenter, Han and Malatesta (2010) provide two additional mechanisms of SWF activism:

1. Anticipation and preferential treatment regarding governmental policy changes, which might be designed to positively impact firms in which government-connected SWFs hold a stake.
2. "Network transactions", which allow target firms to enter into major business agreements with other firms under the influence/participation of the same SWF.

The work of Shleifer and Vishny (1986) on large shareholders corporate governance and control is often taken as the starting point to study SWFs activism. The authors' theory is that large shareholders have incentives to engage in monitoring activities and use their position as blockholders to decisively remove poorly performing executives. From this viewpoint, SWF acquiring large stakes might play an active role in corporate governance. Active blockholders behaviour has been observed for other type of funds, among them SWF-similar pension and hedge funds, and has been found to favour significant increases in target firm performance (Brav et al., 2008; Klein and Zur 2009; Ferreira et al. 2010). Conversely, blockholders might seek objectives that do not concur with shareholders' value maximisation and tend to extract private benefits of control.

Dewenter, Han and Malatesta (2010) provide a notably complete description of the problem posed by SWFs investor activism and its impact on performance. They assume that SWFs impact on firms is characterised by a trade-off between the monitoring and lobbying benefits versus tunnelling and expropriation costs of blockholders. SWFs, as large investors, engage in monitoring activities that create positive expectations in the market, explaining the already mentioned increase of target firms' stock price around

the announcement date of the deal. However, as Shleifer and Vishny (1997) noted, dominant shareholders tend to extract private benefits of control, thus expropriating wealth from smaller shareholders, a position also found in La Porta et al. (2002). To match these apparently conflicting observations, they elaborate a non-linear model of the effects of investment on firm value as a function of transaction size: value increases due to monitoring effects until transaction size reaches a critical level, over which firm value starts to decline as expropriation costs become larger. Using cumulative abnormal returns (CAR), they proof the model significant also for SWFs, finding that transaction share size threshold is placed at around 40% (see Figure 6). Interestingly, this non-monotonic behaviour is observed to be inverse when divestments are considered, showing that partial SWFs divestments are related to negative expectations, while large or total divestments are positively perceived.

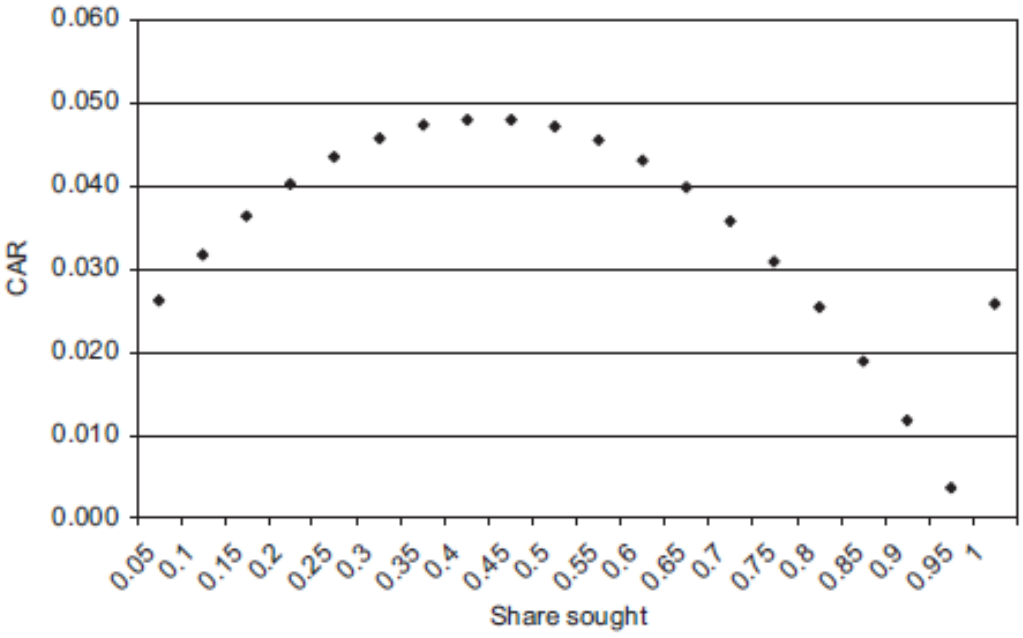

Figure 6. Cumulative abnormal returns as a function of transaction size (Dewenter, Han and Malatesta, 2010)

Impact on long-term performance

To assess whether SWFs investment effectively impacts operating performance, a long-term perspective must be taken since effects on operating performance tend to be slower than those on firm value (stock prices). Existing literature shows mixed results regarding SWFs target firms' performance in the long run.

Sojli (2010) finds that SWFs foreign target firms experience an increase in sales in the years after SWFs' investment, together with an increase in government-related contracts. From this observation, it is guessed that government-related contracts might be one of the main mechanisms through which SWFs' investments induce improved long-term performance. Based on existing literature, the author exposes four reasons for which SWFs might be interested in providing contracts to their foreign targets:

1. To extract know-how.
2. To increase competition and efficiency in the local market.
3. To obtain certification for the domestic market.
4. To exploit insider information.

Additional evidence for a positive impact on both firm value and operating performance can be found in the work of Fernandes (2009).

Contrarily, Bortolotti et al. (2010) find that two-year returns are negatively affected by SWFs investment, especially when they acquire a large stake. Going into detail, Bortolotti, Fotak and Megginson (2015) find that both sales growth and ROA show a negative evolution after SWF investment, in correlation with SWFs engagement in corporate governance, i.e. taking board seats. This is related with the concern about political interference, found to be a further reason for performance deterioration given that several SWFs belong to non-democratic or authoritarian countries with weak governmental control mechanisms. In the case of such funds, the acquisition of high

stakes is often interpreted as a symptom of political interference. According to this logic, considering political distance between home and host country in terms of democratic quality might help clarify the impact of political interference in SWF investment. This issue will be looked at in the analytic part of this work.

Conclusion

As a summary, it must be said that existing literature on SWFs' impact on firms do not provide clear conclusions. However, some general conclusions can be drawn.

Concerning short-term impact, expected monitoring effects of SWFs as large shareholders are related to its tendency to increase firm value around the announcement date of the deal. Despite this fact, these effects might be offset by factors like fear of political interference and transaction size.

Generally speaking, impact on performance in the long-run is deemed to be negative, due to the fact that political interests (naturally biased towards social welfare maximisation) often deviate management from their objectives.

Finally, SWF activism appears to be a key factor for explaining different impacts on firm performance. As Bortolotti, Fotak and Megginson (2015) formulated, SWFs can act in three different ways which are translated into different effects on performance:

- If they take an active role and monitoring effects are dominant, effective management is enhanced and a higher overall performance can be expected, compared to that of comparable private funds.
- If they take an active role but underlying interests manage to impose a political agenda, home country government's goals prevail over profit maximisation. This

could obviously bring a deterioration of performance and value, in comparison with comparable private funds.

- If SWFs as investors take a predominantly passive role in corporate governance, results in terms of operating performance are expected to be worse than those of comparable private investors. From the point of view of this work, this is especially relevant in the case of foreign investment, where investor activism is limited either by the lower influence that governments can exert abroad or the fear of raising political interference controversy.

3. Distance as a driver of cross-border investment performance

The goal of this work is bringing together the topics of SWF impact on operating performance and the concept of distance, in order to draw some conclusions on how the SWF investment – performance relationship is affected by distance when SWFs invest abroad. In order to do so, this chapter provides a brief recap on the concept and measurement of distance in IB research. Then, it goes through a literature review on previous research on the relationship between distance and performance in cross-border investment. By doing so, it builds a base for the case for SWFs on which later data analysis will try to shed some light.

The concept of distance in IB

The concept of 'distance' has been and continues to be one of the main topics of International Business research. During the last decades, a great amount of studies have used it to better explain some international business phenomena, such as patterns in the selection of foreign markets or the choice of entry modes. The general assumption is that cross-border investment becomes more complex and difficult to manage as the differences between the foreign market and the firm's market of origin increase. Despite the centrality of the topic, no unanimity has been reached when it comes to providing a clear definition.

Literature on the topic shows a lack of clarity when it comes to defining the dimensions of distance. Some scholars have argued that distance originates from differences at the cultural, economic, institutional and geographic levels, among others (O'Grady and Lane, 1996; Ghemawat, 2001). Other scholars have conceptualised distance by focusing

on only one of those dimensions, providing a less holistic definition but significantly reducing the complexity of the concept.

"Psychic distance" has been the most extensively used term by scholars when conducting research on distance in IB. This rather generic term was firstly introduced by Beckerman (1956). In a time where only purely objective economic distance was used, he created the new term in order to consider the influence of subjective perceptions as a moderator to economic distance. This concept set the standard for nearly two decades. During the 1970s, researchers in Uppsala University, Sweden, placed psychic distance at the centre of their multinational enterprise (MNEs) internationalisation theories. Taking Beckerman's idea as a starting point, psychic distance was then defined as "the sum of factors preventing the flow of information from and to the market", including "differences in language, education, business practices, culture and industrial development" (Johanson and Vahlne, 1977; Johanson and Wiedersheim-Paul, 1975). However, most of the empirical conceptualisations of psychic distance arising from this definition focus primarily on cultural differences, especially those using Hofstede's (1980) cultural dimensions. The index developed by Kogut and Singh (1988) is a clear example of this approach, which effectively equates psychic distance to cultural distance.

The present work follows the widely spread practice of using the term psychic distance as a generic way of referring to distance in the context of IB studies. Therefore, both forms "distance" and "psychic distance" can be taken as equivalent terms in the pages that follow.

Measurements of distance

The variety of definitions of distance has resulted in a variety of indicators being used in the literature. The first attempt to use distance as an indicator in IB research only included geographical distance (Carlson, 1974). This has usually been considered as a too simplistic approach. However, some recent research suggests that geographical distance could be a better antecedent to perceived psychic distance than cultural distance (Håkanson and Ambos, 2010).

Most operationalizations of psychic distance constructs found in the literature can be classified into three broad categories (Sousa and Lages, 2011).

The first category includes researchers (e.g. Fletcher and Bohn, 1998; Sethi et al., 2003) who have used the index proposed by Kogut and Singh (1988) or any other method based on Hofstede's (1980) cultural dimensions. The assumption behind this approach is that psychic distance and cultural distance are considered to be perfectly equivalent. This was the dominant approach during the last quarter of the 20th century. However, in recent years it has been highly criticised by authors such as Sousa and Bradley (2006), who defend the existence of conceptual differences between both terms which would justify different measurement methods. Indeed, indicators based on national culture dimensions do not consider differences in education, language, level of industrial and economic development, as well as political and legal systems (Dow, 2000).

A second category of psychic distance measurements are developed from national level indicators (e.g. Brewer 2007). They are characterised by two elements. Firstly, the indicators are usually derived from publicly available data. Secondly and most importantly, it assumes that given a pair of countries the distance between any pair of firms from such countries is the same, regardless of the firms' individual characteristics.

Despite the fact that this approach is probably the most objective of all, critics have argued that objective indicators are not enough. According to a perceptual definition of psychic distance (Prime et al., 2009), this approach would fail to capture the individual level bias introduced by the decision maker and other subjective differences (Dow and Larimo, 2009; Whitelock and Jobber, 2004).

In support of the aforementioned perceptual nature of the psychic distance construct, researchers have developed a third category of indicators based on directly asking for the decision makers' estimation of distance towards a foreign country. Some examples of operationalisation of psychic distance measurements according to this approach can be found in the work of Klein and Roth (1990), as well as Sousa and Bradley (2005; 2006).

The relationship between distance and performance

As a consequence of globalisation, cross-border investment and M&As have become increasingly achievable. However, they have simultaneously brought out difficulties and costs of integration when actors from different national backgrounds need to engage in the same project. To tackle this phenomenon, a notable volume of academic research has taken on the concepts of distance to explain the performance outcomes of international ventures.

According to a part of the literature, theoretical and empirical evidence suggests that cross-border acquisitions generally perform worse than domestic deals. As an example, Moeller and Schlingemann (2005) find that cross-border acquisitions performed by U.S-based firms show significantly lower performance than domestic transactions, considering both stock returns and operating performance. Several papers support the idea that cultural differences are the main cause for failure in international acquisitions

(King et al., 2004). Actually, cultural distance is by far the most used distance concept in studies about cross-border M&As.

However, we are still far from reaching unanimous conclusions regarding the relationship between cultural or national differences and investment performance, partly because of different methodological and conceptual approaches. Apart from a few researchers who claim that this relationship cannot be judged as either fully positive or negative (e.g. Reus and Lamont, 2009), a majority of researchers are far from conclusive. The main theories concerning performance-distance relationship are discussed here.

Negative impact of distance

Apparently, the intuitive expectation would be that national differences and performance are negatively related. This view is shared by an already old research stream which underlines various factors to prove the incompatibilities and challenges of engaging players from diverse cultures (e.g. Buono, Bowditch, and Lewis, 1985; Jemison and Sitkin, 1986). Indeed, claims that cultural differences build barriers to integration and generate costs are commonly found in management literature (Weber et al. 1996; Kogut and Singh, 1988; Luo, 2002; Ahern et al, 2015).

As cultural (or psychic) distance increases, it is more likely that differences will arise in organisational practices, management styles, decision-making, human resources management and ethical codes (Slangen, 2006). Supporters of the negative impact of distance claim that the greater the dissimilarity between cultures, the more difficult it will be to integrate and transfer those practices. As Weber et al. (1996) put it, large cultural differences are related to weaker management commitment and cooperation,

even posing a threat for efficient use of synergies. Relatedly, *cultural ambiguity* within firms as defined by Buono, Bowditch and Lewis (1985) is boosted by differences in management styles (Datta, 1991).

Positive impact of distance

Despite the academic tendency to advocate for the negative impact of distance on cross-border performance, evidence does not always support such a view. Some researchers claim that deals between an acquirer and a target from distant countries or cultures might perform even better than in the case of cultural similarity (e.g. Shimizu et al., 2004; Stahl and Voigt, 2008; Chakrabarti et al., 2009). Earlier papers by Larsson and Risberg (1998) and Morosini et al., (1998), insisted in the complementarity of some differences between cultures. The latter study includes a quantitative analysis showing that target firms perform better with increasing distance, concluding that "national culture enhances cross-border investment performance by offering access to various new routines and repertoires, embedded in the target company's or the acquirer's national culture".

In a study based on a sample of 119 cross-border acquisitions performed by Chinese firms between 1995 and 2008, Qian et al. (2017) find that acquisition performance is positively impacted by national culture distance in the three years of post-acquisition. No significant effects on performance are found for the first and second year after acquisition, meaning that this result makes a case for a positive long-term impact of distance on performance, complementing earlier results by Steigner and Sutton (2011). From the perspective of strategy, a possible explanation for a positive impact of distance could be that nationally distant investors could enhance target firm competitiveness by

providing it with a unique set of norms, routines and business practices that other companies in the host country cannot imitate. As Barney (1991) put it, culturally diverse firms can enhance their performance by building mechanisms to combine different routines and repertoires and implement "the best out of both cultures".

Gomez-Mejia and Palich (1997) insist in the idea of benefits coming from potential combination of practices, since cultural heterogeneity widens managers' viewpoints, options and solutions to critical business problems and therefore enhance decision-making.

Contingency approach to the impact of distance

Given the conflicting views on the impact of distance on performance, some authors have assumed that there is no simple answer to the question whether acquirers will face poor or strong performance in distant countries. Instead, they have elaborated on theories that identify moderating factors that interact with distance depending on the context. In other words, they provide contingent answers.

Reus and Lamont (2009) claim that distance is a "mixed blessing" for investment performance, because it increases the learning potential, but also impedes the integration needed for the learning to take place. For them, effects of cultural distance depend on understandability and communication capabilities within the firm, particularly within management.

Azar and Rian (2014) contingent approach focuses in the role of innovation. They check the relationship between psychic distance, innovation and performance, using both financial and strategic assessments of the later. Results shows that psychic distance does not have a significant direct effect on firm performance, but rather a positive indirect effect through innovation. From this view, it can be argued that despite assuming the

challenges posed by distance in successfully achieving positive performance effects, impediments can be overcome in the presence of technological and organisational innovation.

Findings by Evans et al. (2008) on the mediating role of entry and marketing strategies in the relationship between psychic distance and firm performance are aligned with these views. However, the fact that the scope of the study is limited to the retailing sector means that their conclusion might not be generalisable to the broader perspective that is taken in the present work.

The case for SWFs

There is very scarce academic work explicitly focused on how distance can be used to better understand investment performance. At most, some of the studies on SWFs impact on performance check for differences between domestic and cross-border investment, typically finding that cross-border acquisitions favour negative performances (Rubera, 2019). However, this might be in contradiction with some of the literature on international M&As which has been cited.

With this in mind, the analysis that follows hereunder is aimed at providing a first exploration into what "contingency theorists" would denominate a moderating role of distance on SWFs targets' performance. In other words, the question is whether impact on target firms' performance is in any way different as distance between SWFs' home country and the host country varies. And if so, what distance measurements among the variety used by IB are to be considered better predictors?

4. The role of distance on SWF performance impact. An exploratory analysis

The aim of this chapter is to provide a data-based approach to the relation between SWF investment and target firms' operating performance, placing the focus on the role played by distance. In the first place, an explanation on the origin and elaboration process of the used database is provided. Secondly, data is analysed in a descriptive and exploratory manner, trying to envisage any hidden relations between distance and SWF performance effects, when different distance measurements used in IB are considered.

Database

The following paragraphs provide a detailed description of the database that will be used for the later analysis that will try to answer the questions set in the previous chapter. The database was created as a synthesis of two already existing ones, to which some other data was added. Because of this circumstance, both original databases will be briefly described. Finally, the process of creation of the new database by treating and combining the original ones will be detailed, together with the description of the new database.

SWF Investment Database

The first of the databases used in this work was created in 2018 by two MSc students at Politecnico di Milano, Julien Airoldi and Anne-Sophie Marie Luisa Lidgard, for their thesis work on SWF investment strategies.

The data was extracted from Bureau van Dijk's Zephyr database, and contains information about deals made by 31 funds, a majority of them being SWFs and some of them pension funds. The database contains a total number of 2461 deals made between

2000 and 2017, and 60 variables coming from the Zephyr database and other sources (Melbourne Business School, Sovereign Wealth Funds Institute, World Bank, among others). For every deal, variables relate to the following aspects:

- Description of the deal (date, value, type of deal…).
- SWF characteristics (type of fund, transparency index, country…).
- Home country data (economic and industrial development scores, political indicators, macro region…).
- Host country data (economic and industrial development scores, political indicators, macro region…).
- Target firm characteristics (business sector).
- Distance indicators between home and host countries (Dow Psychic Distance, democracy, education…).

Panel Database

The second database used in this work was created in 2019 by a MSc student at Politecnico di Milano, Eugenio Rubera, for his thesis work on the effect of SWF investment on target firms' performance.

The Panel Database (as it was named by its author) takes the Investment Database as a starting point and combines it with information on SWFs deals from the Orbis platform, also from Bureau van Dijk. To be able to capture the effects of acquisition on performance, the author selected the deals that took place between 2010 and 2014 and target firms' performance data for the period ranging from 2009 to 2016, meaning that availability of data for at least the two years before and two years after the deal is ensured for all the deals. As a result, each fund is represented by 8 rows (period 2009-2016), for 29 variables are provided (Table 2). The variables provide information on:

- The deal (year of acquisition, deal type, domestic/cross-border, final stake…)
- The acquiror fund (typology, transparency score…)
- The target firm (company age, sector, ROE, total assets…)

	VARIABLE	DESCRIPTION	DATA TYPE
1	Deal	Number of the deal (order)	Whole number
2	DealNumber	Unique identification code of the deal (from BvD)	Whole number
3	Target BvD ID Number	Identification code of the target firm	Text
4	Target Name	Name of the target firm during the deal	Text
5	Year	It takes values from 2009 to 2016	Whole number
6	Company age	Age of the target firm	Whole number
7	Acquisition	1 if the acquisition happened in that year or following, 0 otherwise	Whole number
8	Deal type	Minority stake, capital increase, institutional buy-out, acquisition or joint venture	Text
9	Stake acquired	% of acquisition of the deal into account	Decimal number
10	Cross border	1 if the target firm's and the fund's countries are different	Whole number
11	BvD Major Sector	Name of the target firm sector	Text
12	NACE Code	Univocal code identifying the target firm's sector	Whole number
13	Date of incorporation	Year in which the company was founded	Whole number
14	IPO Date	Date of the Initial Public Offering	Date (dd/mm/yyyy)
15	Number of companies in the corporate group	If the target company is part of a group	Whole number
16	Listed	1 if the company is listed, 0 otherwise	Whole number
17	Target Region	Macro region of the host country	Text
18	Typology of Fund	Sources of funding of the fund as defined by the SWF Institute (Pension, Commodity, Non-commodity)	Text
19	SWF Dummy	1 if the fund is a SWF, 0 if it is a pension one	Whole number
20	SWF Region	Macro region of the acquiror fund	Text
21	Final Stake	Cumulated stake acquired (in that deal plus the previous ones, if any)	Decimal number
22	Dummy previous participation	1 if the fund had a previous participation in that firm, 0 otherwise	Whole number
23	SWF Name	Official name of the SWF	Text
24	Truman Transparency	Transparency score of the acquiror fund as calculated by Truman (2012)	Decimal number
25	No. recorded subsidiaries	Number of recorded subsidiaries	Whole number
26	No. recorded shareholders	Number of recorded shareholders	Whole number
27	ROE (%)	Financial measure	Decimal number
28	Total Assets	Financial measure	Decimal number
29	Dow index	Psychic distance measurement	Decimal number

Table 2. Panel Database variables (Rubera, 2019)

Final Database

The database used in this work has been elaborated mainly by combining variables from both the Investment and the Panel databases, so that the relevant information for the subsequent data analysis is included.

The steps followed to elaborate the final database are:

1. Identification of variables of interest from each database. On a general basis, the approach has been to obtain variables describing the 766 deals, including information on SWFs and target firms, from the Investment Database. From the Panel database, operating performance (ROE) is the most relevant data that has been included.
2. Construction of a panel-structured database, identical in format to the Panel database, so that time-evolving variables are introduced for each deal.
3. Filtering of the database to keep only cross-border deals.
4. Addition of the geographical distance variable, consisting in distances between capital cities found in the GeoDist Database. This database has been elaborated by CEPII[6], a French centre for research and expertise on the world economy attached to the French Prime Minister's services.
5. Treatment of missing values for ROE variable. Generally, missing values have been interpolated according to a linear trend. Deals for which no ROE values are provided have been removed, as well as deals for which ROE was available for only one year (not being possible to interpolate).

[6] http://www.cepii.fr/CEPII/en/publications/wp/abstract.asp?NoDoc=3877 (April 2020)

The resulting database contains information for 511 deals distributed across 4120 rows and 20 columns, corresponding to the following variables:

	VARIABLE	DESCRIPTION	DATA TYPE
1	Deal	Number of the deal (order)	Whole number
2	Deal Number	Unique identification code of the deal (from BvD)	Whole number
3	Year	It takes values from 2009 to 2016	Whole number
4	Acquisition	1 if the acquisition happened in that year or following, 0 otherwise	Whole number
5	ROE (%)	Return-on-equity (operating performance)	Decimal number
6	SWF country code	SWFs' home country ISO 2-digit code	Text
7	Host country code	Target firm's country ISO 2-digit code	Text
8	Countries combined code	Concatenation of the two previous codes	Text
9	Cross border	Y if the target firm's and the fund's countries are different (only cross-border deals are included)	Text
10	SWF Region	Macro region of the SWF (acc. UN geoscheme)	Text
11	SWF funding source	Sources of funding of the fund as defined by the SWF Institute (Pension, Commodity, Non-commodity)	Text
12	Target firm region	Macro region of the host country (acc. UN geoscheme)	Text
13	Type of deal	Minority stake, capital increase, institutional buy-out, acquisition or joint venture	Text
14	Geo distance	Geographic distance measurement	Decimal number
15	Psychic distance	Psychic distance measurement (Dow)	Decimal number
16	Language	Linguistic distance measurement (Dow)	Decimal number
17	Democracy	Degree of democracy distance measurement (Dow)	Decimal number
18	Industrial development	Industrial development distance measurement (Dow)	Decimal number
19	Education	Level of education distance measurement (Dow)	Decimal number
20	Religion	Religious distance measurement (Dow)	Decimal number

Table 3. Final Database variables

Most variables can be classified in three major groups, depending on whether they describe the deal, the SWF or the target firm:

- Deal-related: deal ID numbers, acquisition, ROE, type, distance measurements
- SWF-related: country, region
- Target firm-related: country, region

Variables *Year* and *Acquisition* provide the possibility to capture performance time-evolution and to discriminate between ante- and post-acquisition periods, respectively.

Descriptive and exploratory analysis

Descriptive analysis of the database

The following pages contain a descriptive analysis of the database, with the aim to understand the nature of its information and as a preparation for the subsequent analysis.

As it has already been said, the database is structured so that each of the 511 deals is characterised by a number of variables that allow to characterise them according to several categories.

If classified by type, minority stake acquisitions account for an overwhelming majority of the deals, representing an approximate 88% of total deals. As Figure 7 shows, they add up to 450, followed by capital increase operations with 35 deals. Institutional buy-outs, majority stake bids and joint ventures are practically anecdotal. Given controversies around SWFs' activities, this distribution might reflect SWFs tendency to keep a low profile when operating abroad, so that concerns about an aggressive and politically-motivated strategy are avoided.

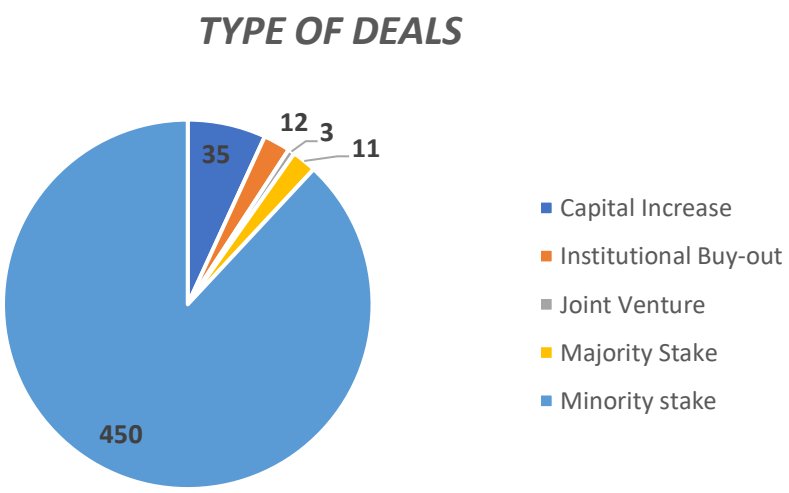

Figure 7. Number of deals by type

Regarding the dates in which deals took place, the number of deals clearly increases throughout the 2009-2014 period (Figure 8), with the only exception of 2011, when it suffered a moderate downturn. Despite not providing any revealing insight with regards to performance, it does reflect the growth that SWFs' operations have experimented and continue to experiment to this day. If 2009 is not considered, having just one anecdotal deal, the number of deals has multiplied by three and a half during the period of study.

Figure 8. Distribution of deals by year

With respect to SWFs, the database is dominated by funds located in Western Asia countries, followed by the rest of Asian countries. Together, SWFs located in Asia as a continent account for the 60% of all SWFs included in the database. This distribution (Figure 10) is quite similar to the actual distribution for all existing SWFs, something that speaks well about the representativity of this sample of 20 funds. Both North America and Europe are home to a 10% of SWFs, with Oceania and Northern Africa completing the list with an approximate 5% each.

As far as diversity of funding sources is concerned (Figure 9), 40% of the funds are funded with revenues from commodity sales, while 35% are non-commodity funded. Pension funds account for just 25% of the sample, meaning that they are outnumbered in a 3 to 1 ratio. Discrimination between SWFs and Pension Funds will not be considered in the subsequent analysis, since both groups present very similar characteristics as international investors and, therefore, a divergent impact on performance will not be checked.

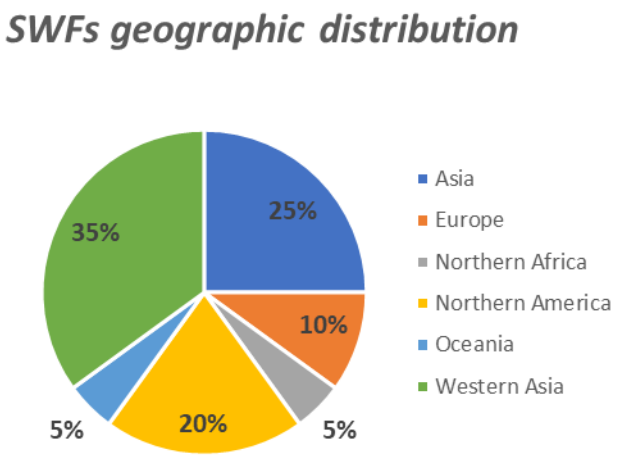

Figure 10. SWF geographic distribution

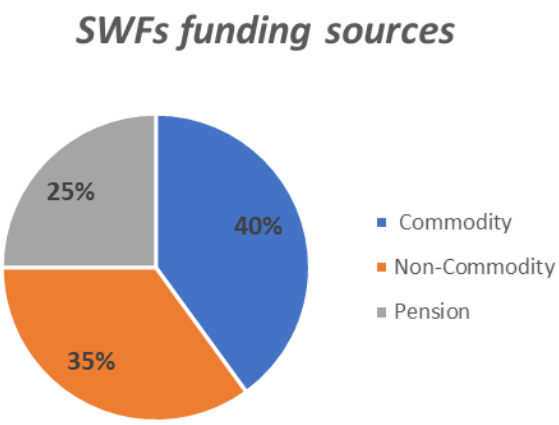

Figure 9. SWFs by source of funding

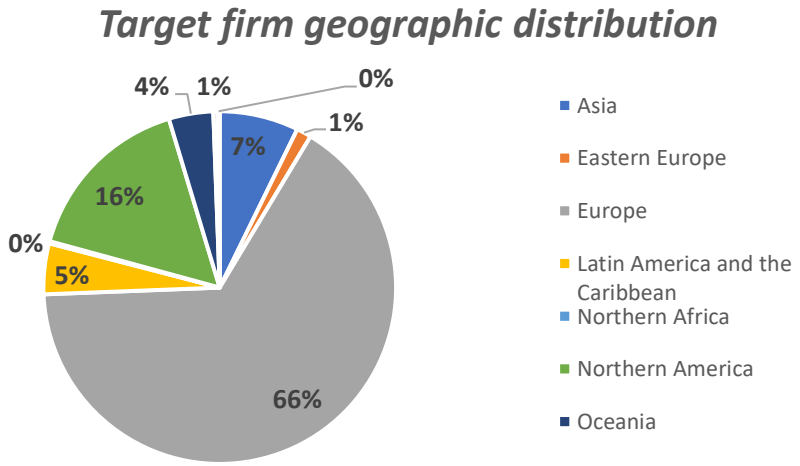

Figure 11. Target firm geographic distribution

An identical analysis to that of SWFs is provided for target firms' geographic distribution in Figure 11, showing that Europe is the major recipient of SWFs investment. The region receives up to 66% of the total acquisitions, with North America in second place accounting for 16%. This figures show that an overwhelming 82% of the studied deals are directed towards the most economically developed regions. The combination of this observation with SWFs' geographical distribution (Figure 10) is reflecting one of the most particular traits of SWFs: the inversion of traditional investment flows, so that funds belonging to emerging economies invest great sums into firms based in developed nations.

To end the descriptive analysis, some descriptive statistics are provided with respect to the numeric variables of the database (operating performance and distance measurements):

Variable	Mean	St.Dev	Min Value	Max Value	Range
ROE (%)	2,31	72,82	-859,49	595,88	1455,37
Geo Distance (Km)	3923,2	4544,3	315,5	19175,60	18860,0
Psychic Distance	1,3585	1,44	0,00	6,84	6,85
Language	-0,6931	1,41	-3,87	0,53	4,39
Democracy	0,37	0,59	0,00	2,06	2,06
Industrial Development	0,45	0,49	0,00	2,06	2,06
Education	0,43	0,41	0,00	2,14	2,14
Religion	-0,48	0,79	-1,55	1,28	2,83

Figure 12. Numeric variables descriptive statistics

Exploratory analysis

The following analysis uses the variables of the described database to address the questions posed on the previous chapters regarding distance as a moderator of SWFs impact on target firms' operational performance.

Simple statistical tools are used, mainly a mix of descriptive analytics and some simple regression models, as the goal is to explore the data by disentangling the dimensions of distance. It could be said that it aims to uncover potential relations behind the data to set the ground for subsequent analysis based on complex data models and hypothesis testing.

The variables used in the analysis are:

<table>
<tr><td>Dependent variable</td><td colspan="3">ROE (%)</td></tr>
<tr><td rowspan="6">Potential explicative variable or drivers</td><td colspan="3">Acquisition (dummy)</td></tr>
<tr><td rowspan="5">Distance measurements</td><td colspan="2">Geographic</td></tr>
<tr><td rowspan="4">Psychic</td><td>Industrial development</td></tr>
<tr><td>Education</td></tr>
<tr><td>Democracy</td></tr>
<tr><td>Language</td></tr>
<tr><td>Religion</td></tr>
</table>

Table 4. Variables used in the data analysis

The impact of acquisition

The first matter that needs to be treated in this analysis is whether operating performance of target firms' actually decreases after receiving SWF investment. This is a widespread conclusion among academic research. Indeed, this impact was also analytically measured by Rubera (2019) using the same database. His econometric analysis showed that SWFs' (including pension reserve funds) have a negative impact on target firms' performance, especially when deals are cross-border.

Figure 13 shows the operating results of target firms, represented by ROE, controlling for ante- and post-acquisition differences. Results seem to be quite clear with regards to the decrease in ROE after acquisition, with an overall average ROE showing a strong positive result before the deal (7,85 %) and dropping to a negative average after the acquisition (-2,51%). Given that only cross-border deals have been included in the final database, this results are aligned with findings on the strengthened negative impact of SWFs cross-border acquisitions.

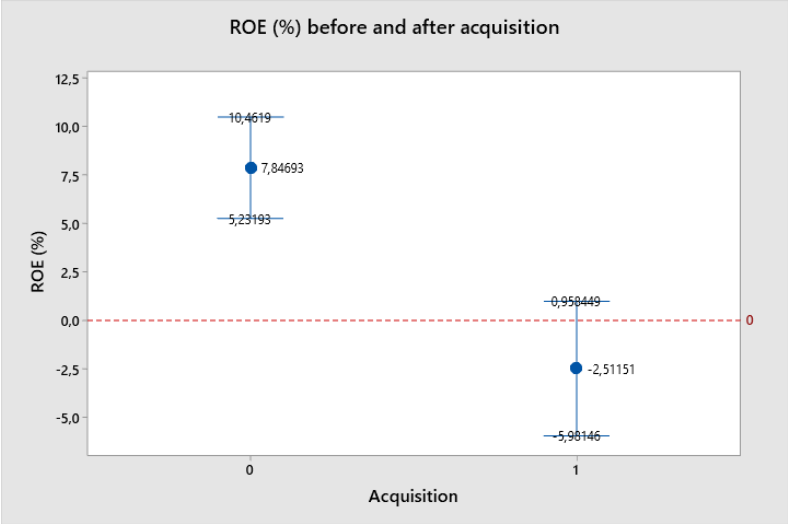

Figure 13. Interval plot of ROE controlled by ante- and post-acquisition

An additional observation comes from looking at the 95% confidence intervals provided in the graph, which not only confirm the aforementioned difference in results before and after the deal (intervals for the mean do not overlap), but also illustrates the fact that post-acquisition performance shows higher variability. This is very much aligned with literature's remarks on the difficulty of predicting effects on performance, reflecting the complexity of the problem. We will take it as an invitation to further dig in the determinants of the observed behaviour by turning to the role of distance.

The role of distance

Once that the starting point of performance being negatively affected by acquisition has been made, we will try to get some insights on the role played by distance. The objective

is to deduce if distance can partially explain the variability observed in post-acquisition performance.

To do so, the methodology is based on plotting the results of ROE against different the different IB-common distance measurements included in the database, while always controlling for the changes between before and after acquisition situations.

Operating performance vs psychic distance

Psychic distance is one of the most commonly-used distance constructs in IB. Theoretically, it represents a well-balanced measurement of distance, according to the widespread view that distance in IB must be understood as a multidimensional concept.

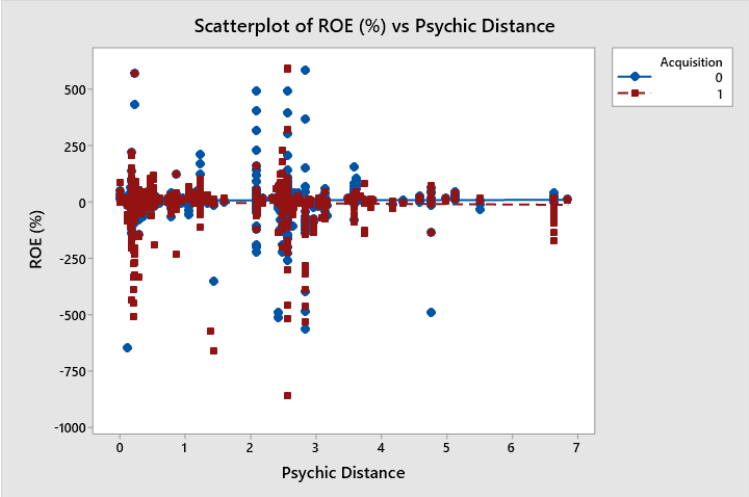

Figure 14. ROE against psychic distance, controlled by ante- and post-acquisition.

Term	Coef	SE Coef	T-Value	P-Value	VIF
Constant	7,35	2,34	3,14	0,002	
Psychic Distance	0,36	1,18	0,30	0,762	2,23
Acquisition					
1	-7,58	3,14	-2,42	0,016	1,91
Psychic Distance*Acquisition					
1	-2,08	1,58	-1,31	0,189	3,08

The analysis is based on the fact that if psychic distance were not to play any significant role, post-acquisition relation of ROE with psychic distance would show no different tendency than the same relation before the deal. The latter is a purely statistical correlation check with no causal implications, since the relation only makes sense once an acquisition has taken place, meaning that the ante-acquisition relation will be taken as a distance-neutral behaviour of ROE. The representation of ante- and post-acquisition ROE with respect to psychic distance provided in Figure 14 shows no distinguishable difference in the pattern in which ROE behaves as psychic distance changes. This is

further confirmed by a simple linear regression showing the decrease in performance after acquisition, while psychic distance is not significantly interacting with acquisition.

Operating performance vs geographic distance

The previous methodology is repeated for geographic distance. In this case, the simple regression model attached to Figure 15 shows an interesting significant interaction between acquisition and geographic distance. According to this, target firms located in geographically distant countries with respect to the SWF's country of origin see their performance especially diminished after acquisition. However, both the scatterplot and the small regression coefficient show that this effect is very subtle, despite being statistically significant, meaning that major differences cannot be solely explained through geographical distance.

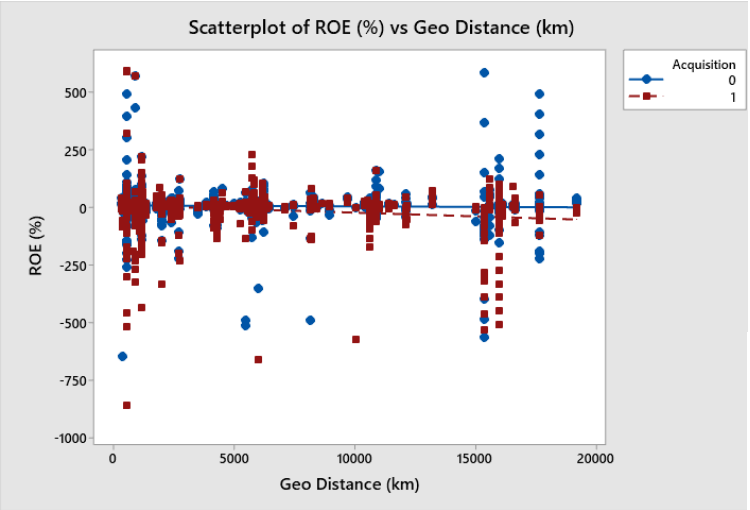

Figure 15. ROE against geographic distance, controlled by ante- and post-acquisition

Term	Coef	SE Coef	T-Value	P-Value	VIF
Constant	9,54	2,15	4,44	0,000	
Geo Distance (km)	-0,000434	0,000356	-1,22	0,223	2,09
Acquisition					
1	0,74	2,96	0,25	0,803	1,74
Geo Distance (km)*Acquisition					
1	-0,002802	0,000493	-5,68	0,000	2,85

Disentangling the dimensions of psychic distance

It has been shown that psychic distance as a multidimensional construct does not seem to play any role in the dynamics of post-acquisition performance. Nevertheless, this fact does not invalidate the possibility to dig into the components of psychic distance to analyse the effects of individual dimensions of distance, as they reflect differences between countries on very different aspects.

This is done by proposing a regression model for performance including the five dimensions of distance found in the database, and their interactions with the acquisition dummy. Similarly to the previous analysis, interaction between distance measurements and the acquisition variable are the important variables to look at, while main effects are overlooked. The variables of interest are:

Dependent variable	***Explicative variables of interest***
ROE (%)	*Acquisition*
	Acquisition
	*Democracy * Acquisition*
	*Industrial Development * Acquisition*
	*Education * Acquisition*
	*Religion * Acquisition*
	*Language*Acquisition*

Table 5. Variables of interest in the analysis related to psychic distance

Having said that, this analysis is concerned with multicollinearity issues when including all distance measurements. The results of the correlation Figure 16 show that all dimensions are strongly correlated, a situation which is considered in the model as explained in the following paragraphs.

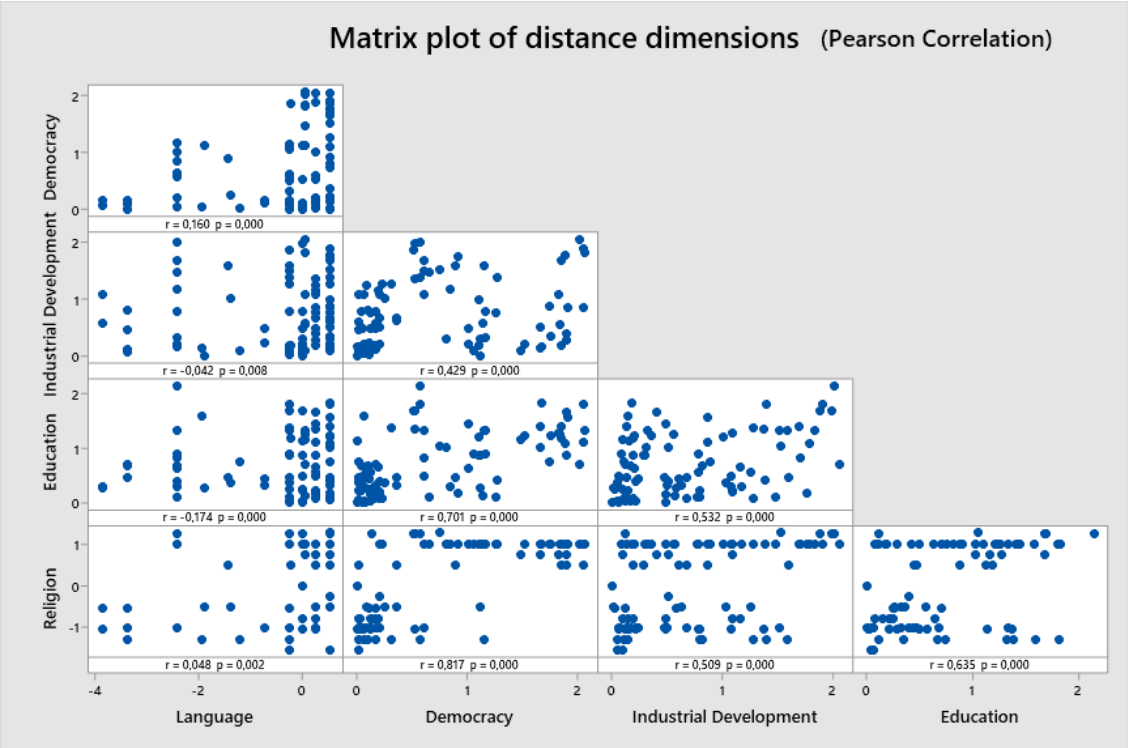

Figure 16. Matrix plot and correlation analysis of distance dimensions

The results of a first regression included in Table 7 show that only the interaction between linguistic distance and acquisition is statistically significant. However, the results cannot be judged as reliable due to the already mentioned multicollinearity, as high VIF factors reflect. In order to avoid this problem, a commonly used strategy is followed, consisting in removing non-significant variables with high VIFs. In an iterative process, non-significant variables are removed and the model is recalculated.

The resulting model, shown in Table 6, is reduced to two significant factors: acquisition and the interaction between language and acquisition. This results confirm the general findings that SWFs investment has a negative impact on target firms, while showing a surprising positive influence of linguistic distance. This means that growing language differences seem to play a moderating role on negative performance results after SWFs acquisitions. Possible interpretations are discussed in the following chapter.

Term	Coef	SE Coef	T-Value	P-Value	VIF
Constant	4,74	4,63	1,02	0,306	
Language	-0,78	1,24	-0,63	0,531	2,41
Democracy	1,54	5,76	0,27	0,789	9,18
Industrial Development	5,58	4,26	1,31	0,190	3,34
Education	-4,81	6,47	-0,74	0,458	5,56
Religion	-2,81	3,73	-0,75	0,450	6,85
Acquisition					
1	-10,17	6,37	-1,59	0,111	7,92
Language*Acquisition					
1	3,69	1,80	2,05	0,040	2,56
Democracy*Acquisition					
1	-5,64	7,86	-0,72	0,473	11,96
Industrial Development*Acquisition					
1	2,99	5,77	0,52	0,605	4,65
Education*Acquisition					
1	3,95	8,98	0,44	0,660	9,04
Religion*Acquisition					
1	-3,10	5,23	-0,59	0,553	8,33

Table 7. Results of the first regression model

Term	Coef	SE Coef	T-Value	P-Value	VIF
Constant	5,35	2,03	2,64	0,008	
Language	-0,50	1,11	-0,45	0,654	1,92
Religion	-4,07	1,43	-2,85	0,004	1,00
Acquisition					
1	-8,29	2,54	-3,27	0,001	1,26
Language*Acquisition					
1	3,04	1,61	1,89	0,059	2,06

Table 6. Results of the definitive model

Results and discussion

The results from the analysis can be summarised in the following four observations:

- SWFs acquisitions have a negative impact on target firms' operating performance.
- Growing geographic distance is statistically correlated with a deterioration of performance after the acquisition, although the magnitude of the effect is minor.
- No evidence is found for the role of psychic distance as a single multi-dimensional construct.
- Linguistic distance between SWFs' country of origin and target firms' country has a moderating effect on the negative impact of acquisition.

The observed negative impact of foreign SWFs investment on ROE is not surprising, as it is aligned with previous findings on the long-term effects on performance (Bortolotti et al., 2010). Deteriorating performances can be related to SWFs introducing political interests into firm management, therefore deviating the focus from the standard objective of profit maximisation. This will happen when SWFs exert their influence to pursue the home country government's international agenda (Bortolotti, Fotak and Megginson, 2015) or in the case of investment having an asset- and knowledge-seeking motivation.

Additionally, negative results can also arise due to SWFs behaving as large shareholders to expropriate minority shareholders wealth, resulting in poor performances, a situation expected to be especially true when it comes to cross-border investment (Shleifer and Vishny, 1997).

Moving on to the rest of the results, this work's findings on the role of different distance measurements on SWF investment on performance might be qualified as surprising, judging by apparently contradicting outcomes.

Firstly, statistically significance found for geographic distance contrasts with the lack of significance found for psychic distance. It is a common assumption in the literature that, in order to be used in IB research, distance measurements need to be combined into multi-dimensional indicators as in the case of the psychic distance construct being used here (Dow and Karunaratna, 2006) . Contrarily to that view, this results contribute to restore the validity of geographic distance as an effective indicator when accounting for distances in IB studies, as it has been pointed out by a rather small part of the literature (Håkanson and Ambos, 2010). However, the magnitude of the effect is found to be very low, meaning that it might usually go unnoticed and be of limited application.

Secondly, a result is found for the role of linguistic distance, according to which performance after SWFs investment would moderate its magnitude as differences in language grow. While a direct effect being caused by linguistic distance alone might look questionable, language differences can be interpreted as an indicator of wider cultural differences. The conclusion then would be that cultural distance has a positive moderating role on SWFs impact on performance. Indeed, cultural heterogeneity has been seen as a source of improved performance when studied over a broader set of deals performed by investors not limited to SWFs (e.g. Steigner and Patton, 2011). However, it might be noted that positive impact of cultural differences is related to the transfer of new managerial viewpoints and best practices embedded in the funds' national culture into the target firm governance (Gomez-Mejia and Palich, 1997), a situation that is only possible if an active investor role of SWFs is assumed.

5. Conclusions

The relevance of sovereign wealth funds (SWFs) in international financial markets has significantly grown during the last decades with the establishment of new funds and the sustained increase of their assets under management.

Public opinion and the media have taken the lead as generators of concerns about their activities and potential links to political and strategic interests, while academic research on the topic shows an important proliferation of studies mainly aimed at understanding the nature, diversity, investment strategies and governance practices of SWFs.

This work is aligned with the still scarce literature on the impact of SWFs on target firms' performance, which has generally focused on the short-term effect on firm value, i.e. stock price returns around the deal's announcement date. The approach taken is an attempt to study the impact on operating performance in relation with the concept of distance when SWFs invest abroad.

An exploratory analysis of a set of cross-border deals made by SWFs from 2009 to 2014 provides contributions to the existing literature at two-levels.

Firstly, it confirms the already existing evidence on the negative performance effects of SWFs cross-border investment. This has evident managerial and policy implications, as it justifies concerns about SWFs. One the one hand, firms' managers and corporate governance organisms should be aware of the motivations of SWFs interested in acquiring a stake of the firm, and especially monitor the behaviour of funds that already hold a significant stake to avoid deviations from the goal of profit maximisation. On the other hand, policy makers might find in this results a reason to justify the promotion of restrictive policies on foreign SWFs investment, arguing that they favour performance

inefficiencies into the domestic economy, as well as the introduction of closer scrutiny and requirements in financial regulations.

Secondly, the study of the dynamics of performance related to the distance between SWFs and their target firms contribute to quite an unexplored approach. The main conclusion is that some individual dimensions of distance are found to play a moderating effect on the impact on performance.

Growing geographic distance between home and host countries tends to further deteriorate performance. However, the small magnitude of this relation represents a limitation, as effects of geographic distance might be hardly observable.

In the case of psychic distance, the multi-dimensional construct used in the analysis does not explain the decrease in performance, although linguistic distance as an individual measurement is found to exert a surprising positive impact. If linguistic distance is to reflect differences at the broader cultural level, this contributes to previous findings on the beneficial effects of cultural diversity on firm performance, by expanding them to the context of SWFs. It must be added, though, that such effects can only be achieved under the assumption that SWFs engage in an active role as investors with the aim to influence firms' management.

This result can be the base for further work on distance as a determinant for performance variability in SWFs acquisitions. The role of cultural differences could be further explored by including alternative measurements of cultural distance, such as the classical country-level constructs proposed by Hofstede (1980) and Dow (2006), and the perceptual approaches of authors like Sousa and Bradley (2006).

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